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Unclaimed Property

Unclaimed property is an area that is increasingly becoming a compliance headache for larger corporations, the authors of the new third edition of Bloomberg BNA's Portfolio 1600—Unclaimed Property told Bloomberg BNA in an interview. The authors, John Coalson, Michael Giovannini, Matt Hedstrom, Kendall Houghton and Ethan Millar of Alston & Bird, gave their thoughts on new developments in unclaimed property and discussed the process and ideas behind the new edition of the portfolio.

Bloomberg BNA Q&A With the Authors of the New Third Edition of Bloomberg BNA's Portfolio 1600—Unclaimed Property





JOHN COALSON, MICHAEL GIOVANNINI, MATT HEDSTROM, KENDALL HOUGHTON AND ETHAN MILLAR, INTERVIEWED BY ALEXANDER DOWD

Kendall Houghton is a partner in Alston & Bird's Washington, D.C. office and leads the firm's state tax and unclaimed property practice; John Coalson is a partner in Alston & Bird's Atlanta office; Ethan Millar is a partner in Alston & Bird's Los Angeles office; Michael Giovannini is a senior associate in Alston & Bird's Charlotte office; and Matthew Hedstrom is a senior associate in Alston & Bird's New York office.

BLOOMBERG BNA: With the new version of the Uniform Unclaimed Property Act coming out, what approach to gift cards do you think that the ULC will take?

ETHAN MILLAR: I can start with a little bit of background on what's already happened with the ULC and the treatment of gift cards specifically. Originally, a number of organizations, including the American Bar Association, submitted comments to the ULC recommending that the revised Uniform Act include a provision generally exempting gift cards on the basis that the escheat of gift cards, at least where the gift cards are redeemable for merchandise or for services and not for cash, would be inconsistent with the basic doctrine of unclaimed property that's become known as the Derivative Rights Doctrine. This doctrine generally provides that the state has no greater rights to the property than

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the owner of the property because the state, when it escheats unclaimed property, does so as a custodian on behalf of the owner and for the purpose of returning that unclaimed property to the owner.

And so, for a gift card that's not redeemable for money, it wouldn't make sense to require the issuer of the card to escheat money to the state and then give that money to the owner, who wasn't entitled to it in the first place. However, NAUPA opposed these recommendations and recommended that the revised act include a provision requiring escheat of gift cards similar to what's currently in the 1995 act.

The first draft of the revised uniform act that came out in February did include NAUPA's recommendation on that point. There was additional discussion of that issue at the ULC drafting committee meeting in late February, and the drafting committee ultimately decided to include alternative provisions in the next version of the draft revised act: one provision that would require escheat of gift cards and another provision that would exempt gift cards from escheat. Thus, it would then be at the option of each state adopting the revised act to choose which of those alternative provisions the state wants to include.

As you may expect, we have concerns with that approach for a number of reasons. First, any rule that requires the escheat of money with respect to gift cards that are redeemable only for merchandise or services is contrary to the purposes of the act, violates federal laws, and is inconsistent, again, with the approaches of the American Bar Association, the National Retail Federation, and other organizations.

Second, this approach also raises pretty serious uniformity issues. There has been a trend over the last 20 years or so, since the 1995 act was adopted, to exempt gift cards from escheat. In fact, over 30 states now have exemptions for gift cards to some degree or another. Giving states an option to exempt or escheat gift cards obviously does not reflect this trend and thus has the potential for moving us backwards rather than forwards in terms of increasing uniformity.

MICHAEL GIOVANNINI: States like Oregon present a more interesting question, as Oregon does not affirmatively exempt or escheat gift cards/gift certificates. It would not be a surprise to see the state consider foregoing the proposed default provision if it adopts the new act in light of the recently proposed legislation.

We can only hope that Tennessee is unique with respect to its silly legislative proposal, which would restrict the sale of gift cards to face-to-face transactions. Luckily, it does not appear that this legislation will advance in the legislature.

BLOOMBERG BNA: We've addressed this somewhat, but should the Uniform Unclaimed Property Act follow the same idea as the New Jersey elimination of all consumer data collection when it comes to these stored value cards? And I think if the ULC continues to follow this trend of exempting gift cards and other stored value cards from unclaimed property, then that would be moot, would it not?

MILLAR: Yes, absolutely. There's really no reason for the uniform act to include any kind of data collection requirement if the cards wouldn't be subject to escheat in the act in the first place. But even if they keep an optional provision that requires the escheat of gift cards and then some states adopt it, certainly we would recommend that the uniform act not include any kind of consumer data collection requirement. I think we've all seen numerous issues that have come out of that as a result of the New Jersey situation, insofar as that kind of requirement imposes substantial and unnecessary costs on card issuers and may also be opposed by some consumers who don't want to provide that kind of information when they buy gift cards.

It also raises a fundamental issue of inserting into the Unclaimed Property Act a provision that is not intended to regulate unclaimed property but is instead intended to impose a substantive regulation on gift cards. Such a regulation would be outside the scope of what unclaimed property laws should be addressing. And perhaps it is for that reason that, at least to my knowledge, no one has suggested inclusion of such a consumer data collection requirement in the revised act.

BLOOMBERG BNA: Moving along to third-party contingent-fee audit firms. This was a topic of debate at the drafting meeting in February. Should the Uniform Law Commission specifically address this process for contracting with these third-party firms, or do you think that this would be preempted by state laws that are already in place that generally address government contracts with private entities?

MATTHEW HEDSTROM: I'm going to start with the answer to this question, or some thoughts on this question, and then welcome the other members of the team to weigh in—especially those that were sitting at the table for the debate around this issue. First, we'll talk about the general issues with third-party contingent fee audits, some of the concerns, and the differing views and then we can talk about the impact of competing state laws or state regulations regarding outsourcing of an audit function to a third-party. The answer to the precise question of whether the ULC should address this issue: I think the answer is, in some respects, they should address it, given that there are considerable concerns from the holder perspective with the use of contingent fee auditors, especially where those auditors are given very wide latitude in determining the manner and method in which to conduct the audit.

With that said, I think our view, or at least my view, and others can weigh in when they have a chance on this point, is that it is unlikely that the ULC will meaningfully address the holders' collective concerns, given the views of the states, as articulated by NAUPA and other stakeholders, that these types of arrangements are necessary to administer the unclaimed property laws, and that these types of audit firms and practices generate considerable revenue for the various states. The states have articulated a number of reasons why these arrangements are necessary and/or invaluable to the administration of unclaimed property laws. From the state's perspective, they view these arrangements as ''necessary'' primarily due to the cost savings in the short- and long-term. There's very little expense or cost outlay in conducting these audits. States don't have to pay cash up front to get the audits underway and only are paying when there's a recovery by the contingent fee auditors. The states also contend that without the contingent-fee arrangements their ability to administer their respective unclaimed property laws would be crippled due to staffing constraints as well as substantive expertise. On this latter point, I think it's fair to say that states have not outlined or adopted any sort of uniform training of unclaimed property auditors; contrast that with the state tax function where there is a focus on

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auditor training, and a purported significant focus on training.

States also contend that multistate contingent fee audits are necessary, given that, in certain instances, the recovery for some states (lower population states quite often) can be quite minimal and thus paying for that type of audit out of pocket would be infeasible. For those of us that also practice in the state tax arena as well, the contingent fee audit practice is in stark contrast to general state tax audit procedure where contingent fees/third-party audit arrangements are rare. I would take the position that, despite the states' insistence that these arrangements are necessary, given the types of fees that states have paid to third-party auditors over the course of the last 10, 15 years or so, it seems there should be some reasonable way to bring the function ''in-house.'' It bears mentioning that some states, specifically New York, rarely outsource their audit function and are able to achieve holder compliance and conduct their own audits.

The views that I've just outlined are ones that, I think, are adopted by COST, TEI and other organizations that speak out against/raise concerns with these types of arrangements. So what should the ULC do at minimum? Given the fact that it's pretty unlikely that ULC and the states will agree that these types of agreements ought to be prohibited, I think there are probably some key issues that need to be addressed. At a minimum, the ULC should address, in some fashion, the significant concerns, one of which is the compensation structure. Obviously, given that there's a contingent-fee element, auditors are incentivized to take aggressive positions and potentially take aggressive positions particularly with respect to exemptions. There are other ways to structure the audit arrangement in order to limit this incentive; at very least states could move to a modified contingency fee, if not just an hourly arrangement.

I think contract audit firms often exercise too much control and influence over audits, and there needs to be a renewed focus on state oversight, especially in making critical audit decisions, application of statutory exemptions and other state-law based decisions. And there needs to be transparency around when the state is actually making those decisions. I also think that there needs to be some parameters put around the qualifications of various audit firms that get into this space. Over the last couple of years, we've seen a number of new entrants to the contingent fee audit space and the more audit firms that become involved the more difficult it becomes for states to exercise necessary oversight and the less standardized the audit practices become.

KENDALL HOUGHTON: John, I would invite you to comment on this issue, since you and I wrote an article way back in 1998 on this very topic.

JOHN COALSON: Indeed, Alex, as Kendall just alluded to, we wrote an article back in '98 or '99. It was around that time. And ironically, not much has changed since then. But one of the things that we pointed out in that article relates to the second point that Matt mentioned above, and that is the need for oversight of the contract audit firms in restricting the exercise of influence, control, and discretion that the audit firms have on critical decisions regarding the application of the law in the audits.

We really don't think that this is just a matter of good practice. It's really necessary in order for a contingent fee audit to pass constitutional muster under the Due Process Clause. If states don't exercise meaningful control over the conduct of the audit, including making critical decisions about the application and interpretation of the law, as opposed to reviewing data and determining facts, then the conduct of the audit and any proposed assessment of liability is really constitutionally suspect. And so that is one of the areas in which at least I, personally, feel the states do not do a good enough job, and it's partly a result of these being multistate audits. States just sign on and then they wait for the results. And far too often, they exercise no meaningful effective control and limit the discretion of the auditors to fact finding as opposed to interpretation and application of the law to the facts.

BLOOMBERG BNA: On a related note, the *Temple Inland* case in Delaware is proceeding after the court agreed at that Temple Inland could survive the motion to dismiss and could make a case for due process violation. And you've previously stated, I believe it was in one of your alerts on unclaimed property, that you all think that Temple Inland is likely to emerge victorious in this. So how do you think this could affect the decision-making process for the ULC when it comes to addressing these third-party audits in the new version of the Uniform Unclaimed Property Act?

HOUGHTON: I'll address the question and then invite more comments from my coauthors. Certainly, as Matt just laid out in very detailed fashion, the concerns with the use of third-party audit firms are being addressed by the Uniform Law Commission, and to the extent that your question about the Temple Inland case is relevant to that consideration, I think we've covered it.

However, there is another aspect to the contract audit firm practices that poses very serious due process and fairness concerns for holders. As has been fully illustrated in the Temple-Inland litigation in the Delaware federal District Court, the contract audit firms utilize very aggressive estimation techniques to establish liability for periods where a holder lacks complete and researchable records. The numbers in the Temple-Inland case were certainly eyebrow-raising for many who read the complaint and realized that you had this multiplication factor that was certainly not linear when Kelmar employed its estimation techniques for purposes of establishing Temple-Inland's Delaware unclaimed property liability. It wouldn't be unreasonable to surmise that if estimation of unclaimed property liability were held to be unconstitutional, then the motivation for being in the business of providing audit services to the state of Delaware would presumably substantially evaporate, because the very significant component of the liability upon which those firms are being compensated would disappear.

That might render the contract auditing line of business less attractive or feasible to any number of firms that are currently involved, but I don't think, personally (and I again invite John, Ethan, and Matt's views on this) that the Uniform Law Commission is waiting for the Delaware District Court or the courts in general to opine on the constitutionality of estimation in order to tackle the question of what audit firms are doing in this regard. And the firms are clearly utilizing estimation techniques based on the fact that the '95 act and the '81 act referenced the contracts of estimation and the states

have authorized them to use estimation techniques, and in particular, Delaware, which is the most popular choice of domicile state.

So the problem to be solved is not an audit firm problem. It's more a question of what is appropriate in terms of addressing holders' records retention requirements, what happens when they don't retain those records — both the concept of estimation and the technique of estimating liability are being addressed right now in section 20 of the revised uniform act. Notably, we're seeing a shift in terms of the drafting committee's thinking by virtue of its removal of the reference to the use of estimation as a *penalty* for failure to keep records, but I think it's a little early to predict precisely what the Uniform Law Commission is going to do in that regard. While I'm not touching on the constitutional aspects of the Temple-Inland case, we recently addressed that set of concerns in one of our advisories and will probably touch on that at the end of this interview because you've inquired where the potential sea changes may be.

BLOOMBERG BNA: Any further comments on the Temple Inland case? Then we'll move on to life insurance and the use of the social security death master file by insurance companies when it comes to reporting unclaimed property proceeds. I know this was a topic of lively debate at the February drafting meeting for the ULC, so how do you think that the ULC will address this question?

COALSON: As to the ULC, it's unclear what the drafting committee will end up recommending with respect to the escheat of life insurance proceeds. We believe that provisions like the NCOIL model legislation are matters of regulation of the business of insurance. And if they're enacted, they should be in the state's insurance code and be enforced by the state's insurance department as part of the overall regulation of the business of insurance rather than in an unclaimed property law. However, at least in the discussions at its February meeting, the drafting committee indicated an inclination to include within the revised Uniform Unclaimed Property Act, some obligation for life insurance companies to periodically search the DMF or comparable databases and to investigate any matches to attempt to determine if their insureds have, in fact, died and attempt to obtain proof of death and locate beneficiaries and obtain a claim for the policy proceeds. At least up to now, we don't think the drafting committee has indicated an inclination to go further as NAUPA has suggested and equate the identification of a match on such a database with, quote, ''proof of death'' sufficient to begin the running of the period of presumed abandonment even if the insurance company is unable to confirm the death of the insured and obtain proof of death after a reasonable effort.

So we would like to see the committee simply retain the existing provision from the 1995 uniform act with respect to unclaimed life insurance proceeds and if additional provisions are needed to improve the industry's claim payment practices, they should be enacted as a part of the state insurance regulatory statutes. For unclaimed property purposes, the period of abandonment shouldn't begin to run until the policy proceeds are, in fact, due and payable, under the terms of the policy and under applicable insurance laws.

BLOOMBERG BNA: On a related note, I remember this was also discussed at the drafting meeting. If I remember correctly, these potential new rules regarding the death master file would only apply to policies that are signed and paid for after this rule was in effect should the ULC adopt something similar.

COALSON: I mentioned in my previous comment that the National Conference of Insurance Legislators, or NCOIL, has adopted model legislation that would require licensed insurance companies to periodically compare the insureds under their life insurance policies in force against the DMF and to investigate apparent matches and try to confirm whether the insureds have died, et cetera. The NCOIL model legislation has been enacted in a number of states. I think it's up over 15 now, maybe a few more. Only West Virginia has, thus far, imposed such requirements as part of their unclaimed property law.

Because the requirements represent a clear change in the law and impose obligations on insurance companies with which they've never previously had to comply and that weren't taken into consideration in consideration with the underwriting and pricing of policies sold in the past, we think they should be applied only to new policies written after such requirements become law. Even if the obligation to search the DMF and attempt to locate beneficiaries who appear to be deceased is applied to existing policies, certainly any attempt to require insurance policy proceeds to be reported as unclaimed property absent the receipt of due proof of death should not be applied retroactively. We believe any attempt to apply such change in the law retroactively to existing insurance policies would likely be unconstitutional.

BLOOMBERG BNA: Moving to a question that was somewhat discussed by, I believe it was Kendall, at our roundtable a few weeks ago, should the Federal Government intervene through legislation to bring about some kind of real uniformity in escheat for unclaimed property, and is there any likelihood of this issue actually gaining traction in Congress?

HOUGHTON: I will tackle this question. The US Supreme Court established federal common law in its ruling in Texas v. New Jersey, Pennsylvania v. New York, and Delaware v. New York. Each of those rulings established or reaffirmed the jurisdictional rule for escheatment of unclaimed property. And as you may know, federal common law is uniform due to the Supremacy Clause and its effective preemption of inconsistent state law. Still, as we discuss in the portfolio, the court explicitly stated in Delaware v. New York, in 1993, that Congress may allocate abandoned property among the states without regard to this court's interstate escheat rules. Indeed, as discussed in the portfolio, Congress has exactly done that with respect to uncashed travelers checks and money orders, in the Disposition of Money Orders and Travelers Checks Act which it enacted in 1976, I believe. The doctrine of federal preemption is often encountered in the unclaimed property arena and we've devoted a fair amount of real estate in the revised portfolio to discussing express and implied preemption of state laws, including state unclaimed property laws, by various forms of federal statute, federal agency regulation, as well as the federal common law rules I just mentioned.

One of the Supreme Court's most recent decisions holding that federal law preempts the state's exercise of

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unclaimed property law jurisdiction, would be New Jersey v. the United States Department of the Treasury, a 2012 decision issued by the Third Circuit Court of Appeals. That court held that pertinent to the doctrine of federal preemption, state laws are invalid if they conflict with an affirmative command of Congress. On the other hand, state agencies attempt to limit the application of federal preemption.

With regard to the question of whether Congress is going to wade into this territory for the purpose of imposing uniform rules on the states, and to what extent, my view is that it's doubtful for a few different reasons. First, we have the Uniform Law Commission attempting the very feat of introducing and/or reinforcing uniformity of law in the unclaimed property arena. And we've already talked about obstacles to attaining uniformity among the states in this field of law.

Secondly, Congress may not be a particularly well-positioned broker of difficult political deals, given the polarization we see with regard to other state tax legislative efforts, including the Streamlined Sales and Use Tax Act, BATSA (the Business Activity Tax Simplification Act), and other sales and use tax legislative proposals.

I guess the third obstacle that I see is the question of what would the goal of federal legislation be? Is it to change jurisdictional priority rules? If so, the loser would clearly be Delaware and other preferred domicile states which enjoy the second jurisdictional priority default benefits. Or would the goal of federal legislation be to prevent certain practices, such as the use of estimation or the use of contingent fee auditors? We certainly should expect states to undertake very hefty lobbying efforts and to assert federalism or separation of powers arguments in that regard. It really seems, taking the Disposition of Money Orders and Travelers Checks Act as the best example of a successful federal preemption and uniformity effort, that a narrowly scoped bill probably has the best chance of passage. But again, I think I rated the chances of success as being slim to none when we were speaking in our state tax roundtable dialogue a couple of weeks ago. Ethan, John, Matt, do you have a different view or do you agree with me on that?

MILLAR: I would agree. I think that at least in the current political environment, the likelihood of comprehensive federal legislation in the unclaimed property area is, as you suggest, Kendall, slim to none. But perhaps in the future, it could be an option. And I think if it was done properly, it could really clear up a lot of the ambiguities in the current act, and could of course address the uniformity issue once and for all. So it could be a great benefit, I think, both to holders and owners of unclaimed property.

Just to mention some of the issues that you alluded to a moment ago, Kendall, in terms of why this is an issue or why it's necessary for there to be federal legislation even though we have federal laws already that preempt at least to some degree the state escheat laws. One example is the third priority rule or the rule under which states can escheat property based on where the debt arose. Holders have been arguing for years that such a rule is unconstitutional under the federal common law rules that you mentioned, Kendall, but nonetheless it took a decision of the Third Circuit to finally address that issue. And even with that decision, and others like it such as the Tenth Circuit's decision in American Petrofina, state organizations like NAUPA continue to argue that these decisions should be narrowly construed and that it's still appropriate to have a third priority rule or other priority rules in the Uniform Unclaimed Property Act that are different than the rules that are set forth by the Supreme Court in those three cases.

And then you see other instances in the ERISA context and other areas where some states try to narrowly construe federal rules or authorities. Comprehensive federal legislation would, presumably, resolve those issues.

HOUGHTON: Right.

BLOOMBERG BNA: Being that it's been 20 years since the last version of the Uniform Unclaimed Property Act, are there any other kinds of property besides gift cards that the ULC may not have anticipated being issues in unclaimed property, and are there any other blind spots either there or within state laws that might be an issue?

COALSON: Yes, there are any number of things. Any statute that gets drafted that tries to simply address property type by property type what the rules are will be out of date to some extent almost from the time it's passed because the types of property are always evolving. It's a moving target.

I'll mention, for example, the current trends towards the use of payroll cards. Those are typically issued by a bank. Employers transfer the funds to the bank or to the payroll program administrator, which then applies the funds to the payroll card account. Once the funds have been applied, they're in the total control of the employee, and then are available to the employee and under the control of the bank. From our perspective, it's difficult to see why that process is any different than the direct deposit of payroll funds into a bank account and that the holder for unclaimed property purposes would be the bank, and they would have the responsibility for escheating the funds after a period of presumed abandonment that is consistent with a bank account.

Many state administrators, however, contend that, because the nature of the obligation that is satisfied through the transfer of funds is payroll, that somehow those funds should remain the obligation of the employer who would be the holder, and that they would have the shorter period of presumed abandonment that applies to payroll. And frankly, it's something that there's just no answer to under existing law, at least no clear answer. Other kinds of current property would include things like incentive and reward cards. Are those treated as gift cards, or does it matter that they're issued for no consideration to the consumer? We think it does.

Regarding the current trend towards having federal and state benefits be loaded on to cards rather than issued as checks, should they be treated as stored value cards like gift cards, again, when they're really not the same kind of obligation as gift cards? Almost any kind of nonrefundable prepayment for goods or services might be an issue. For example, if I have gone to a sports club, and I could get a personal training session for $100, but instead the club will sell me six personal training sessions for $300 but with a stipulation that I have to use all six within the next six months, but I have no right to a refund so I can't get any cash back. If I've simply prepaid for six personal training sessions with the contractual understanding that if I don't use them all within six months, I lose my right to use them, is there unclaimed property involved there? We don't

think so, but many state administrators would contend that there is.

HSA accounts, Roth IRA accounts, and other types of tax advantage accounts didn't exist in 1995, and if we adopt a new statute in 2016, by 2020, there will be others that don't exist. Virtual currencies, very hot item right now, particularly in the electronic gaming world, totally unclear whether there's any unclaimed property issues involved. One of the points of all this, I think, is that any effort to draft an unclaimed property law that simply tries to articulate every conceivable type of property and what the rule to be is doomed to failure, I think.

Instead, what we need, because of the constant evolution of properties that are potentially covered by unclaimed property laws, we believe there's a real need for neutral principles of law to guide the application of unclaimed property laws to the ever evolving types of property. And the key neutral principle that we believe should control is the Derivative Rights Doctrine. It is that kind of a principle, and we support the ABA, the Unclaimed Property Professionals Association, the Unclaimed Property Holders Coalition, COST, and others who are encouraging the Uniform Law Commission to recognize the Derivative Rights Doctrine as a fundamental guiding principle in the application of unclaimed property laws. We'll see if we're successful. So far they have not shown an inclination to do that and we think it's a mistake. We hope, at the very least, the comments to the act will acknowledge the crucial role that the Derivative Rights Doctrine has played and has been recognized by the courts of almost every state as playing in the application and interpretation of unclaimed property laws as applied to new and evolving types of property.

BLOOMBERG BNA: As we touched on with states like New York moving their audit procedures in-house, most companies have personnel in their tax departments that deal specifically with unclaimed property compliance. Do you think more states should take this approach as well, perhaps by transferring this function from the state treasurer to the state's department of revenue?

COALSON: Well, the first thing I'll say is I'm not certain that the premise of the question is actually true, at least in my experience. It's at least equally likely that the unclaimed property compliance responsibility in companies will be placed in the company's finance group as that it will be in the tax department. Certainly it could be in either place, and is, in different companies. But especially in larger companies that have shared services functions for things like accounts payable and payroll and accounts receivable, I find that the compliance function for unclaimed property is often in the finance area.

It's true that unclaimed property compliance and auditing shares many characteristics in common with taxes. And the tax department in a company is much more likely to have relevant experience both in the preparation and submission of annual reports based on codified laws and the handling of audits. And likewise, within a state, certainly a tax department is going to have expertise and experience in auditing returns and reports, be they tax returns or unclaimed property reports.

Here in Georgia, for example, though, the unclaimed property law has been administered by the Department of Revenue as long as I can remember, I think as long as it's been in the law. I know going back to 1981, which is when I handled my first audit here in Georgia, it's been in the revenue department. But Georgia hasn't ever been a particularly aggressive state in the application of those laws. So wherever it is included, I think one of the key requirements is that there be adequate resources aligned with the function to give the administrator, whoever it is, whether it's in finance or in revenue, the needed resources to effectively audit and enforce the laws. And certainly it could be in the tax department as well as in a finance department.

BLOOMBERG BNA: This is a question for the group. Is there a need for an equivalent commission to the Multistate Tax Commission in the unclaimed property arena, and what might be the advantages or disadvantages of that?

HEDSTROM: Thanks, Alex. It's an interesting question that we have certainly discussed as a group. We think there's absolutely an opportunity for some additional and/or broader oversight over, in particular, the administration of state unclaimed property laws, and as we'll talk about in a second, the audit function, although I think NAUPA may contend that it already serves a similar function that the MTC serves in the tax context.

With that said, we think that there are certain lessons to be learned from the MTC, specifically in the context of the conduct and operation of multistate audits. Although taxpayers and practitioners have legitimate concerns with the structure and operation of MTC audits, the MTC has instituted some sort of control and oversight and states might benefit from a similar type of formalized audit oversight in the unclaimed property context. There is a chain of command within the MTC, it's understood by the taxpayers, and there's a way in which the issues can be formally raised up the chain. In addition, there is a certain level of transparency that's present at the MTC level, that's not present within the unclaimed property multistate audit space.

In addition, the MTC has endeavored to document audit policies and guidelines in its audit manual. And, whether right or wrong, at least in that context, the rules of engagement are established and established uniformly. And so I think in that regard, you raise an interesting question and it bears considering whether some form of centralized audit oversight that the MTC has in the tax is needed in the unclaimed property context.

BLOOMBERG BNA: I suppose our larger, overarching question is: What are the other big trends or potential events might cause a sea change in unclaimed property in the near future?

MILLAR: Right now, some of the most important issues in unclaimed property are finally being litigated in the courts, and so the results of those cases, which could affect virtually every industry, could have a wide-ranging impact both on how unclaimed property laws are applied and how they're enforced. I'll mention four cases right now that are pending and that have potentially groundbreaking effects in the world of unclaimed property.

One of these, which we have already discussed, is the Temple Inland case. That case has raised the fundamental issue of whether and to what extent states have the right to use estimation, and whether estimation can be used to calculate unclaimed property that's owed to

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owners, or whether states can use it as a penalty for failures by holders to retain records of owners of unclaimed property. I understand that trial is set for January of next year, so we may get a decision quite soon on some of these basic issues.

If the court does end up limiting the ability of the state of domicile of the holder to use estimation, then that certainly would be a sea change in the world of unclaimed property. It would most obviously have a drastic impact on Delaware, which derives hundreds of millions of dollars each year from the use of estimation. Such a decision would also have a significant impact on other states that use estimation to escheat a substantial amount of property, such as New York. Interestingly, even if those states are determined to have no right to use estimation, under the secondary rule, it's possible that that could open the doors for other states, in particular the states in which the owners of the unclaimed property are located, to use estimation in the future, perhaps as a penalty for failures by holders to maintain required records in the first place.

Another big issue that's being litigated right now, in *State ex rel. French v. Card Compliant et al.* in Delaware Superior Court, is the issue of whether individuals can bring qui tam actions or whistleblower lawsuits under state false claims acts against companies for alleged violations of state unclaimed property laws. We are representing thirteen of the retail defendants in this case. In our view, these sorts of qui tam suits are simply not permitted by the states' False Claims Acts for a variety of reasons, including that false claims acts apply only where there is a preexisting liquidated obligation, which would not be the case for a potential violation of a state escheat law. Indeed, California courts have rejected such suits on this basis in at least two prior cases. In the next couple months, the Delaware Superior Court will have an opportunity to weigh in on some of those issues.

Hopefully, the Delaware court will, like the California courts before it, reach the right answer and realize that disagreements regarding the application of the escheat laws should be resolved under the administrative procedures set forth in the state unclaimed property laws rather than through false claims acts, which are quasi-criminal statutes that provide for treble damages, recovery of attorneys' fees and other penalties. But if such qui tam actions are allowed to proceed, that could open the floodgates to very aggressive litigation against holders by states and Plaintiffs' firms that are looking to use the leverage of the higher penalties in the false claims act to extract substantial settlements from defendants.

A third big issue that's being litigated right now, in Federal District Court in Massachusetts, is whether states have the right to escheat foreignowned securities. Both holders and owners of foreignowned stock have long argued that the escheat of foreignowned property is unconstitutional, but that issue has never been litigated until now, where we are arguing on behalf of two clients that the states have no right to escheat such property.

The ABA, UPPO (the Unclaimed Property Professionals Organization) and other organizations have agreed that the escheat of foreign stock is unconstitutional. And the current draft of the revised Uniform Act also provides that states do not have the right to escheat such property. If the federal district court agrees with that position, that could deal another substantial blow to Delaware's use of unclaimed property as a revenue source, as Delaware also derives a significant amount of revenues from escheat of foreign property.

A final big issue that I would like to mention today that is currently being litigated is a basic issue of derivative rights. Our firm is representing the putative holder, Bed Bath & Beyond, in cases pending in California, New Jersey and Connecticut, and the question is whether the state can require the escheat of money with respect to merchandise return certificates, or store credits, that are redeemable only for merchandise and not for cash.

We have already favorably resolved this issue with many other states at the administrative level.

However, these cases are important because they involve core issues of statutory construction, as to whether the unclaimed property laws should be construed to require escheat of money when the holder's only obligation is to provide merchandise. These cases also raise constitutional issues, such as whether the escheat of money may violate the takings clause, substantive due process or federal common law. So these cases could have a significant impact in terms of whether holders only have to escheat what they owe to owners, or whether states can go beyond that and require holders to escheat money even though the holders don't have obligations to pay money to owners. This may have implications in many other areas such as used personal training or spa sessions, movie or sports tickets, virtual currency, or anything else you can imagine where it's not a straightforward obligation to pay money.

COALSON: Loyalty points is another one.

MILLAR: Yes, good point.

BLOOMBERG BNA: What, specifically, is special about this new version of Portfolio 1600?

MILLAR: Well, I think a lot has changed since the last version of the portfolio. As we talked about earlier, there have been many, many developments in unclaimed property in the last 15 to 20 years, including major changes in statutory provisions and how states address various types of property ranging from gift cards to securities to insurance. There has also been much more litigation in this area that has clarified, to a certain extent, how the unclaimed property laws apply in certain contexts.

States have also gotten more aggressive, and, as a result, holders have gotten more defensive about unclaimed property issues. And so we've seen new arguments being developed, at the administrative level and in audits and in litigation. The portfolio covers all these developments, including all the different issues that arise in terms of state jurisdiction to escheat, what exactly do the federal common law rules stand for, when exactly does a state have the right to escheat unclaimed property, etc. There have been some great new cases on these issues.

Our portfolio also provides guidance to holders and owners on all the different types of unclaimed property or potential unclaimed property that are out there, including all those gray areas that we talked about, such IRAs, Roth IRAs, HSAs, incentive cards, points programs, and other new types of property where the rules may not be clear. We also dedicated an entire section of the portfolio to identifying all the major defenses that

are available to holders so that holders can better understand their rights. Some of these defenses are statutory, some are constitutional, some are common law, and some are federal law defenses. We really tried to expand the scope of the prior portfolio and make it a comprehensive guide to holders of unclaimed property in particular.

BLOOMBERG BNA: You already mentioned the defenses to escheat section. Are there any other areas of the portfolio where you see potential for development?

MILLAR: I think that it will be very interesting to see what becomes of the Uniform Unclaimed Property Act project. Assuming that the uniform act is in fact adopted and becomes the law in some states, I think it would worthwhile to update the portfolio to discuss how the uniform act has addressed some of these controversial issues. I think a lot of the cases that I mentioned a moment ago that are pending right now—Temple Inland, our Massachusetts securities case, our derivative rights cases, all those issues— involve the potential to really change the landscape in unclaimed property or if not change the landscape, at least reinforce the existing landscape where there's currently sufficient uncertainty regarding the law that holders and states are litigating over these issues. And so however those cases end up, I think they will be newsworthy developments and I think that in any update of the portfolio, we would be wise to address them.

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